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April 7, 1998

David S. Guzy
Chief, Rules and Publications Staff
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P.O. Box 25165, MS 3021
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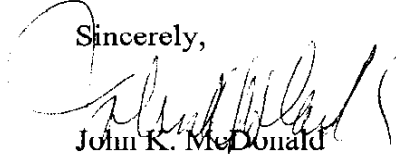
Re: Pennzoil Company Comments on Supplementary Proposed Rule on Crude Oil
Valuation, 63 Fed Reg. 6113 (Feb. 6, 1998).

Dear Mr. Guzy:

Attached please find the comments of Pennzoil Company to the Supplementary
Proposed Rule on Crude Oil Valuation.

If you have any questions, please do not hesitate to call me at (202) 973-0200.

Sincerely,


John K. McDonald

Before the United States
Department of the Interior
Minerals Management Service

Pennzoil Company
Comments on Minerals Management
Service Supplementary Proposal for Valuation of
Crude Oil Produced on Federal Leases
63 FR 6113 (February 6, 1998)
30 CFR Part 206

Pennzoil Company ("Pennzoil") appreciates this opportunity to comment on the supplementary proposed rule for Establishing Oil Value for Royalty Due on Federal Leases proposed by the Minerals Management Service ("MMS"). Pennzoil produces crude oil from federal leases and, as a consequence, has a direct interest in this proposal to alter the method for calculating the value upon which royalty is based. Pennzoil is a member of the American Petroleum Institute ("API") and has reviewed the comments that are being filed by API in this proceeding. Pennzoil has also had the opportunity to review the comments that are being filed by the Independent Petroleum Association of America ("IPAA") and the Domestic Petroleum Council ("DPC") in this proceeding. Pennzoil supports and generally agrees with the comments of API, IPAA and DPC.

It is Pennzoil's position that the federal leases to which it is a party, as well as the regulations that are applicable to those leases, provide that royalty is to be calculated based on the value of production at the wellhead. If there is no market at the wellhead, value is to be determined at the nearest market to the wellhead, minus the cost of moving production to that market. The proposal attacks this standard from both directions, by moving the point for royalty valuation away from the wellhead and by reducing the costs that can be deducted in arriving at royalty value. More specifically:

- The proposal rejects the use of transactions at the wellhead market or lease market benchmarks, except under limited circumstances in the Rocky Mountain Region. Instead, lessees are required to begin the valuation process by tracing production to the first arm's-length sale and then work back to the lease or, where the lessee refines its production, begin with an index value and work back to the lease. The basic problems with this approach are that it is difficult to accomplish, burdensome and it does not produce an accurate surrogate for value of production at the lease.
- If MMS believes that the existing benchmarks are no longer an accurate surrogate for value at the lease, they should be modified or replaced with benchmarks that do


reflect value at the lease. The proposal to trace production to the first arm's-length sale (or begin with an index price for production that is refined) and work back to the lease, does not produce an accurate reflection of value at the lease because it does not reflect the cost of value adding activities between the wellhead and the point of first arm's-length sale or refining.

- The proposal's definition of "gross proceeds" would improperly allow MMS to collect royalties on value beyond the value of production at the wellhead, such as the value added downstream of the wellhead or contract settlement "buydowns."
- The "duty to market at no cost to the lessor" contained in the proposal does not exist in the federal leases to which Pennzoil is a party or the statutes and regulations that are applicable to those leases. This "duty" would have the impact of unlawfully moving the point of value determination from the lease to a downstream market without the lessor sharing post-production value-adding costs.
- To the extent that the MMS insists on determining value at a location away from the lease, Pennzoil believes that the MMS is obligated to share in the costs associated with marketing production.
- The proposal improperly eliminates the use of FERC approved tariffs in calculating transportation allowances, based on a misunderstanding of the laws administered by the FERC, as well as the FERC cases that the proposal cites.

In addition to these general comments, Pennzoil adopts the detailed analyses and discussions contained in the comments of API, IPAA and DPC.

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Respectfully Submitted,



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